

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 319 of 1984

For Approval and Signature:

Hon'ble MR.JUSTICE R.BALIA. and
MR.JUSTICE A.R.DAVE

- =====
1. Whether Reporters of Local Papers may be allowed : YES
to see the judgements?
 2. To be referred to the Reporter or not? : NO
 3. Whether Their Lordships wish to see the fair copy : NO
of the judgement?
 4. Whether this case involves a substantial question : NO
of law as to the interpretation of the Constitution
of India, 1950 of any Order made thereunder?
 5. Whether it is to be circulated to the Civil Judge? : NO
-

COMMISSIONER OF INCOME TAX

Versus

ANNABEN AJAYBHAI

Appearance:

MR RP BHATT for Petitioner
MR MANISH J SHAH for Respondent No. 1

CORAM : MR.JUSTICE R.BALIA. and
MR.JUSTICE A.R.DAVE

Date of decision: 10/05/1999

ORAL JUDGEMENT

1. At the instance of C.I.T. Gujarat I following question of law arising out of its order in ITA 1932/Ahd/79 relating to assessment year 1973-74 has been referred to this court for its opinion:

"Whether, on the facts and in the circumstances of the case, the Appellate Tribunal has been right in law in holding that there was no transfer of capital asset when the assessee contributed as a capital asset when certain immovable properties of the book value of Rs.2,16,519/- to the firm of M/s. Dipak Trading Co. in which the assessee was a partner and consequently, the difference of Rs.21,166/-

credited to the capital account on the basis of market value at Rs.2,67,885/- is not exigible to capital gains tax?"

2. The assessee was a partner in the firm M/s. Deepak Trading Co. She contributed as her capital certain immovable properties of the book value of Rs.2,46,519/- in the said firm. The assessee revalued the said immovable properties at the market value of Rs.2,67,685/-. The difference of Rs.21,166/- was credited to the capital account of the assessee. The income tax officer was of the view that the transaction amounted to transfer of capital asset to the partnership firm by the assessee within the meaning of Section 2(47) of the act and attracts the provisions of Section 45 of the said Act. He therefore computed capital gains arising therefrom. In appeal CIT (Appeals) did not agree with the finding of the Income Tax Officer and deleted the computation made by way of capital gains, in the total taxable income of the assessee. Revenue's appeal was dismissed by the Tribunal. The question has two shades, firstly, whether contribution of an asset owned by a person as contribution of capital to a firm of which he/she is a partner amounts to transfer of such asset by such individual to the firm, secondly, whether such transfer results in capital gains to the partner.

3. Both the questions have been answered by the Supreme Court in Sunil Siddharthbhai v. C.I.T. 156 ITR 509. The court held that where a partner of a firm makes over capital assets which are held by him, to the firm as his contribution towards capital, there is a transfer of asset within the meaning of provisions of the Act of 1961 because the exclusive interest of the partner in the personal assets is reduced, on their entry into the firm into a share interest.

4. The court held that -

"The consideration for the transfer of the personal assets is the right which arises or accrues to the partner during the subsistence of the partnership to get his share of the profits from time to time and, after the dissolution of the partnership or with his retirement from the partnership, to get the value of his share in the net partnership assets as on the date of the dissolution or retirement after deduction of liabilities and prior charges. The credit entry made in the partner's capital account in the books of the partnership firm does not represent

the true value of the consideration. It is a notional value only, intended to be taken into account at the time of determining the value of the partner's share in the net partnership assets on the date of dissolution or on his retirement, a share which will depend upon deduction of the liabilities and prior charges existing on the date of dissolution or retirement. It is not possible to predicate beforehand what will be the position in terms of monetary value of a partner's share on that date. At the time when the partner transfers his personal asset to the partnership firm, there can be no reckoning of the liabilities and losses which the firm may suffer in the years to come. All that lies within the womb of the future. It is possible to conceive of evaluating the consideration acquired by the partner when he brings his personal asset into the partnership firm when neither can the date of dissolution or retirement be envisaged nor can there be any ascertainment of liabilities and prior charges which may not have even arisen yet. Therefore, the consideration which a partner acquires on making over his personal asset to the firm as his contribution to its capital cannot fall within the terms of section 48. And as that provision is fundamental to the computation machinery incorporated in the scheme relating to the determination of the charge provided in Section 45, such a case must be regarded as falling outside the scope of capital gains taxation altogether."

5. In short the ratio of the case is that when the assessee, a partner in a firm, made over to the firm certain shares in a company which were held by him, there is a transfer of shares, but that he received no consideration within the meaning of Section 48, nor did any profit or gain accrue to him for the purpose of Section 45.

6. The apex court made it clear that where the purported transfer of personal asset by the assessee to a partnership is merely a device or ruse for converting the asset into money which would substantially remain available for his benefit without liability to income tax on a capital gain, it will be open to the income tax authorities to go behind the transaction and examine whether the transaction of creating the partnership is a genuine or a sham transaction and even where the partnership is genuine, whether the transaction of

transferring the personal to the partnership firm represents a real attempt to contribute to the share capital of the partnership firm for the purpose of carrying on partnership business or is nothing but a device or ruse to convert the personal asset into money substantially for the benefit of assessee while evading tax on a capital gain.

7. As it is not the case of the revenue that the transfer of immovable property in question was a device or use on the findings of the Tribunal, question referred to us must be answered in terms of the aforesaid decision by holding that though contribution of immovable property by way of capital to M/s. Deepak Trading Co. as its partner by the respondent assessee amounts to a transfer within the meaning of Section 45, its consideration being not possible to determine through the computation machinery provided under the Act. It is not a transaction which fall under Section 48 in respect of which capital gains can be computed and brought to tax.

There shall be no order as to costs.

(Rajesh Balia, J) (A.R. Dave, J)